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3440 Harden Street Ext (29203)
PO Box 4706, Columbia, South Carolina 29240
V/TTY: 803/898-9600
Toll Free: 888/DSN-INFO
Website: www.ddsn.sc.gov

Memorandum

TO: To Interested Parties

FROM: Tom Waring, Associate State Director, Administration *T.W.*

DATE: June 25, 2010

RE: Waiver Respite Changes Required by IRS

Federal IRS compliance requires changes to waiver respite July 1, 2010.

Background:

1. The Internal Revenue Service (IRS) has ruled that respite caregivers for waiver services cannot be independent contractors. This issue came to light in the fall of 2009 when the IRS conducted an audit at one of the DSN Boards. Substantial sanctions were imposed on the Board including monetary fines. It has taken several months to work with various federal and state agencies to identify the correct process to ensure that the respite service provided through the waivers are in compliance with federal and state tax law. Thus, either the waiver recipient/responsible party is the employer of record or the DSN Board/Home Support Provider is the employer.
2. However, Medicaid waiver rules prohibit payment for services directly to the waiver participant/responsible party. Because of this Medicaid requirement, the DSN Board/Home Service Provider will now act as the employer agent and handle the tax reporting on behalf of the family who is the employer of record and/or the DSN Board/Home Support Provider could choose to hire the respite caregivers as agency employees.

Current Procedure:

1. Presently, most of the DSN Boards treat respite caregivers as independent contractors and would issue year-end 1099s for tax accounting purposes, which reported all income

DISTRICT I

P.O. Box 239
Clinton, SC 29325-5328
Phone: (864) 938-3497

Midlands Center - Phone: 803/935-7500
Whitten Center - Phone: 864/833-2733

DISTRICT II

9995 Miles Jamison Road
Summerville, SC 29485
Phone: 843/832-5576

Coastal Center - Phone: 843/873-5750
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Saleeby Center - Phone: 843/332-4104

2. earned by its respite caregivers for the calendar year. This is the tax form that reports income for independent contractors.
3. Since the respite caregiver was an independent contractor, he or she was responsible for payment of federal and state income taxes and the full 15.3% Federal Insurance Contributions Act (FICA). If a respite caregiver earned over \$400, then the full 15.3% FICA is owed to the federal government regardless of any federal or state income tax owed by the respite caregiver.

New Procedures July 1, 2010:

1. Federal and state income taxes are withheld based on information provided on the W-4 submitted by the respite caregiver. Income taxes are withheld based on what the respite caregiver selects as the number of exemptions.
2. Starting July 1, 2010, the DSN Boards/Home Support Provider will report income earned by the respite caregiver as wages. The income will be reported on a W-2 with the DSN Board/Home Support Provider paying the employer share of FICA (7.65%) on behalf of the family. The balance of the FICA tax will be paid by the respite caregiver and deducted from their gross wages. This is the normal practice for any employer/employee relationship.
3. According to federal law, respite service provided in a consumer's home is exempt from federal minimum wage and overtime requirements. Respite provided in any location outside of the consumer's home (for example, the respite caregiver's home) is not exempt from minimum wage and overtime requirements.
4. The minimum wage, if it is required to be paid (currently \$7.25 per hour), is the gross hourly rate prior to any taxes, such as related FICA, federal and state income tax, being deducted from an employee's pay.
5. As an independent contractor, respite caregivers were not eligible for unemployment benefits. But now as employees, they will be eligible for unemployment benefits. Unemployment insurance is an expense of the employer.
6. Workers' compensation insurance is not required to be carried by the employer if an employer has three or fewer employees.
7. The rate of pay for some respite caregivers is being reduced as of July 2010, the respite caregivers will no longer be responsible for the full FICA tax of 15.3% on their earned wages. The difference in actual net pay for the respite caregiver from an independent contractor to an employee relationship should be minimal. This will lessen the financial reporting requirements in regards to tax reporting for the respite caregivers as they are no longer being treated as independent contractors.